

**STATE OF ILLINOIS
ILLINOIS COMMERCE COMMISSION**

COMMONWEALTH EDISON COMPANY :
 :
Petition for approval of delivery services tariffs : **01-0423**
and of residential delivery services implementation :
plan, and for approval of certain other amendments :
and additions to its rates, terms and conditions. :

***REPLY BRIEF ON EXCEPTIONS OF THE STAFF
OF THE ILLINOIS COMMERCE COMMISSION***

**STEVEN G. REVETHIS
JOHN C. FEELEY
Office of General Counsel
Illinois Commerce Commission
160 North LaSalle Street, Suite C-800
Chicago, Illinois 60601
(312) 793-2877**

**Counsel for the Staff of the
Illinois Commerce Commission**

March 4, 2002

Table of Contents

| | |
|--|---|
| INTRODUCTION..... | 1 |
| ARGUMENT | 2 |
| I. Legal Issues and Standards for Decision | 2 |
| A. Substantive Standards and Policies Governing Requested Rates | 2 |
| B. Procedural Issues (e.g., Admissibility) Not Addressed in Specific Arguments | 3 |
| C. Other Policy Issues..... | 3 |
| 1. Impact on Customers | 3 |
| 2. Impact on Cost Based Rates | 3 |
| 3. Impact on the Development of an Effectively Competitive and Efficient Electricity Market | 3 |
| 4. Impact on Future Rate Cases | 3 |
| 5. Impact on Capital Markets | 3 |
| 6. Impact on Distribution Adequacy and Reliability | 3 |
| 7. Additional Policy Concerns | 3 |
| D. Resolution of the Joint Motion..... | 3 |
| II. Revenue Requirement Issues | 3 |
| A. Calculation of Revenue Requirement | 3 |
| B. Selection of Test Year | 3 |
| C. Rate Base..... | 3 |
| 1. Functionalization of Distribution Plant | 3 |
| 2. General and Intangible Plant -- Direct Assignment and Allocation | 3 |
| 3. Known & Measurable Changes to Test Year Plant Balances | 4 |
| 4. Other Adjustments to Rate Base (Non-Plant) | 7 |
| 5. Accumulated Deferred Income Taxes | 7 |
| 6. Plant Adjustments | 7 |
| a. Plant Expenditures for Q2 2001 | 7 |
| b. Proposed Retired Plant | 7 |
| c. Retirements Related to 2001 Replacement Plant..... | 7 |
| d. Accumulated Depreciation Adjustment Related to Overtime and Alleged Premiums Paid | 7 |
| e. Accumulated Deferred Taxes Related to Overtime and Alleged Premiums Paid..... | 8 |
| 7. Prudence of Distribution Capital Investment Costs | 9 |
| a. Effect of Alleged Imprudence on Rates | 9 |
| b. Prudence of Specific Distribution Capital Investments in Rate Base | 9 |
| 8. Other Rate Base Issues | 9 |
| D. Operating Revenues And Expenses | 9 |
| 1. Recommended Operating Income Statement | 9 |
| 2. Operating Revenues | 9 |
| 3. Operating Expenses | 9 |
| a. Functionalization Of Generation, Transmission, And Distribution Expenses . | 9 |
| b. A&G Expenses -- Direct Assignment and Allocation | 9 |

| | | |
|---------|---|----|
| c. | Proposed Known & Measurable Changes to Test Year Expenses..... | 9 |
| (i). | Expense Adjustments Related To Rate Base Adjustments..... | 9 |
| (ii) | “Levelization” Adjustments | 10 |
| a. | Tree Management Expense | 10 |
| b. | Storm Restoration Costs | 11 |
| c. | Reserve for Levelized Variable Storm Damage Expenses..... | 13 |
| d. | Other | 15 |
| (i). | Distribution Salaries and Wages | 15 |
| (ii.) | FERC Accounts 580, 590, 592-594 and 903..... | 16 |
| (iii.) | Salary and Wage Adjustment for General Pay Increases | 16 |
| (iv.) | Adjustments for Post-Test Year “Merger Savings” | 16 |
| e. | Other Proposed Adjustments to Expenses..... | 16 |
| (i) | Exclusion of Incremental Expenses Related to Unicom/PECO Merger ... | 16 |
| (ii.) | Exclusion of Audit-Related Costs | 16 |
| (iii.) | Environmental Remediation Expenses..... | 16 |
| (iv.) | Advertising Costs | 16 |
| (v.) | Bank Commitment Fees..... | 16 |
| (vi.) | Legal Expenses..... | 16 |
| (vii.) | Charitable Contributions & Memberships | 16 |
| (viii.) | Special Projects | 16 |
| (ix.) | Research and Development Costs..... | 16 |
| (x.) | Interest On Customer Deposits | 17 |
| (xi.) | Uncollectibles Expense | 17 |
| (xii.) | Taxes Other Than Income Taxes | 17 |
| 4. | Prudence of Expenses | 18 |
| E. | Cost of Capital | 18 |
| 1. | Capital Structure | 18 |
| 2. | Cost of Debt..... | 18 |
| 3. | Cost of Preferred Stock..... | 18 |
| 4. | Cost of Common Equity | 18 |
| 5. | Overall Rate of Return | 18 |
| F. | Cost Of Service and Rate Design..... | 18 |
| 1. | Cost of Service Study Issues | 18 |
| a. | Marginal Cost Study | 18 |
| b. | Embedded Cost Study..... | 20 |
| 2. | Interclass Revenue Allocation..... | 21 |
| G. | Rate Design..... | 21 |
| 1. | Rider ISS..... | 21 |
| a. | Pricing | 21 |
| b. | Commission Authority to Alter ComEd’s Proposal..... | 21 |
| 2. | Residential Customer Eligibility for Rider PPO..... | 21 |
| 3. | SBO Credit..... | 21 |
| 4. | Metering Service Charge (Credit) | 22 |
| 5. | Rider TS – Transmission Service..... | 23 |
| 6. | 24 Month Return To Bundled Service Requirements..... | 26 |

| | | |
|------------------|---|----|
| III. | Terms and Conditions Issues | 26 |
| A. | SBO Credit Eligibility (Customers With Past Due Bundled Service Balances) ... | 26 |
| B. | Enrollment Issues | 27 |
| 1. | Electronic Signatures | 27 |
| 2. | Term of Service..... | 27 |
| C. | Release and Use of Customer Specific Information | 27 |
| D. | Off-Cycle Or Non-Standard Switching For Residential Customers..... | 27 |
| E. | General Account Agency Issues..... | 27 |
| F. | Value-Added Aggregation Services | 27 |
| G. | Collection of FERC Charges Under DSTs | 27 |
| CONCLUSION | | 28 |

NOW COMES the Staff of the Illinois Commerce Commission (“Staff”) and pursuant to Section 200.830 of the Illinois Commerce Commission Rules of Practice (83 Ill. Adm. Code 200.830), respectfully submits this Reply Brief on Exceptions.

INTRODUCTION

Briefs on Exceptions (“BOE”) to the Administrative Law Judges’ (ALJs) Proposed Interim Order (“PIO”) were filed by Commonwealth Edison Company (“ComEd” or “Company”); the City of Chicago, the People of the State of Illinois, the People of Cook County, and the Citizens Utility Board (collectively, “Government and Consumer Parties”, “GCP,” “GC,” or “GCI”); the National Energy Marketers Association (“NEM”); the Building Owners and Managers Association of Chicago and the Building Owners and Managers Association of Suburban Chicago (collectively “BOMA”); Nicor Energy, L.L.C. (“Nicor Energy”); Midwest Generation, LLC (“Midwest”); TrizecHahn Office Properties Inc., (“TrizecHahn”); AES New Energy, Inc. (“AES NewEnergy”) and Blackhawk Energy Services, L.L.C. (“Blackhawk”) (collectively, the “ARES Coalition”) and the Illinois Industrial Energy Consumers (IIEC).

Staff will respond to certain arguments made by ComEd and the ARES Coalition. Staff’s silence as to other issues raised by the parties in this proceeding should not be construed as acquiescence in or approval of said arguments by Staff.

ARGUMENT

I. Legal Issues and Standards for Decision

A. Substantive Standards and Policies Governing Requested Rates

ComEd takes exception to the PIO's use of the phrase "particular certainty." ComEd argues that such language is not consistent with prior Commission precedent. (ComEd BOE, p. 7) The PIO adopted Staff's out-of-period expense argument regarding "particular certainty". Staff argued that "if out-of-period expenses are not "determinable" with particular certainty, they may not be used to adjust test year expenses or be reflected in rates". (Staff IB, p. 9) Staff's argument addressed the fact that a utility must be able to specify with particular certainty out-of-period expenses used to adjust test year expenses. Once that is done the particular expenses at issue can be judged to determine whether they are reasonably certain to occur, i.e. define the expense, and then determine whether it is reasonably certain to occur. It appears that ComEd has misconstrued Staff's argument as well as the PIO's conclusion in this regard. Therefore, ComEd's exception is inappropriate and therefore, should be disregarded.

- B. Procedural Issues (e.g., Admissibility) Not Addressed in Specific Arguments
- C. Other Policy Issues
 - 1. Impact on Customers
 - 2. Impact on Cost Based Rates
 - 3. Impact on the Development of an Effectively Competitive and Efficient Electricity Market
 - 4. Impact on Future Rate Cases
 - 5. Impact on Capital Markets
 - 6. Impact on Distribution Adequacy and Reliability
 - 7. Additional Policy Concerns
- D. Resolution of the Joint Motion

II. Revenue Requirement Issues

- A. Calculation of Revenue Requirement
- B. Selection of Test Year
- C. Rate Base
 - 1. Functionalization of Distribution Plant
 - 2. General and Intangible Plant -- Direct Assignment and Allocation

Even though the PIO adopted ComEd's position with respect to the functionalization of General and Intangible plant, the Company seeks to strengthen the language on the issue. Sensing the weakness of its position, ComEd proposes the adoption of additional language describing the Company's response to arguments against its proposed functionalization methodology (ComEd BOE, pp. 11-12).

ComEd's proposal presents problems. The Company provides little support in its discussion for the significant language additions it proposes on the issue, nor does it explain whether the proposed additions reflect the lengthy record developed in this proceeding. Thus, ComEd appears to be casting far and wide for some evidence to support what is clearly a deficient ruling by the ALJs on this issue.

The Company is concerned about the discussion in the PIO for good reason. Even though the ALJs adopt ComEd's position on the issue, their discussion in the PIO clearly demonstrates that the evidence supports the labor allocator proposed by Staff and other intervenors. That discussion makes it even more difficult to conceive why the ALJs would support the Company's functionalization methodology.

As a starting point, the Commission should reject these language additions proposed by ComEd. The Commission should then proceed to reverse the PIO's conclusion on this issue and, instead, accept the labor allocator proposed by Staff to functionalize General and Intangible plant to distribution.

3. Known & Measurable Changes to Test Year Plant Balances

Staff and GCI proposed a downward adjustment of \$11,038,000 for plant put into service in the second quarter of 2001 along with the associated adjustments for accumulated depreciation, accumulated deferred income taxes and depreciation. The Company had put a \$126,592,000 estimate of its expected expenditures in its original filing for such plant. Staff asked data requests during its review as to what amount was actually spent through the end of the second quarter and if the plant was indeed placed in service. After an initial response, the Company indicated in a corrected response that

all plant items contemplated to be placed in service as of the end of the second quarter of 2001 were in service and that the expenditures made were \$11,030,000 less than claimed in its filing.

The PIO at page 40, correctly concludes that Staff's adjustment to plant, along with its associated adjustments for accumulated depreciation, accumulated deferred income taxes and depreciation expense, is appropriate.

ComEd objects to the finding in the PIO. (ComEd BOE pp. 15-21) Staff pointed out that ComEd Witness Voltz presented testimony at the surrebuttal stage that an additional \$8,100,000, or a total of \$123,680,000, had been spent on these projects through the third quarter of 2001. Mr. Voltz had even speculated that expenditures were to continue on some unspecified projects in the months to come that may even make the original forecast of expenditures in the filing correct. (Staff RB, pp.7-8) Staff pointed out, and the PIO agreed, that Staff cannot be expected to consider alleged expenditures for rate base treatment without evidence such as invoices, workorders, or even bookkeeping entries. (Staff Reply Brief p. 8) Also, the "evidence" provided by ComEd merely consisted of quoting a dollar figure which is insufficient evidence to determine if plant is used and useful and reasonable and prudent. ComEd argues that Mr. Voltz's testimony must be accepted since it was not impeached, however the Commission is not required to accept as true all evidence that is unrebutted. (City of Chicago v. Illinois Commerce Commission, 15 Ill. 2nd 11, 16 (1958)) Simply because ComEd puts a witness on the stand does not mean that the Commission is obligated to accept that witness's unsupported testimony. The PIO has clearly given ComEd

Witness Voltz's surrebuttal testimony with its unsupported amount, its proper weight in the proceeding.

ComEd continues to assert that it proposes no adjustments for the third and fourth quarters of 2001 or for any period in 2002, and then goes on to claim \$8,100,000 of unsubstantiated expenditures in the third quarter of 2001 and the balance of the \$126,592,000 that will be made sometime in the non specific future. (ComEd BOE p. 14) The PIO properly rejects the Company's contradicting positions. ComEd argues that Staff, at the post-hearing stage, concluded that ComEd needed to support its expenditures, rather than just having the Company mention some dollar amount in its surrebuttal testimony. Since the Company for the first time raised the claim of having additional expenditures in its surrebuttal testimony, Staff did not have an opportunity in its own testimony to respond to ComEd since there was no provision in the schedule for a Staff surrebuttal. That is the only reason that ComEd can make the claim that Mr. Voltz's surrebuttal testimony has gone "unrebutted". (ComEd BOE, p. 18)

It should also be noted that the record lacks any evidence as to what is the proper amount of associated adjustments for accumulated depreciation, accumulated deferred income taxes and depreciation expense related to Mr. Voltz's \$123,680,000 claimed plant in service.

Other than to introduce a new term such as "trailing expenditures on projects" which is not reflected in the record in this case, ComEd's BOE has shed little light to justify a change in the PIO. The PIO should remain as it stands.

4. Other Adjustments to Rate Base (Non-Plant)
5. Accumulated Deferred Income Taxes
6. Plant Adjustments
 - a. Plant Expenditures for Q2 2001
 - b. Proposed Retired Plant
 - c. Retirements Related to 2001 Replacement Plant
 - d. Accumulated Depreciation Adjustment Related to Overtime and Alleged Premiums Paid

The PIO finds Staff's proposed adjustments to plant for overtime and alleged premiums paid to contractors to be unwarranted at this time due to the underlying issue of prudence that is being investigated in Docket No. 01-0664. However, the PIO did conclude that should adjustments be necessary, Staff's depreciation rate is proper and should be used to calculate associated adjustments with any plant adjustments found after the investigation. (PIO, p. 44)

The PIO concludes that Staff's depreciation rate is based upon the best information available. Staff concurs with the PIO.

ComEd disputes the use of Staff's depreciation rate of 3.6% claiming that some composite rate should be used. (ComEd BOE, pp. 22-23) As pointed out by Staff, ComEd Witness Jerry Hill cited unspecified "Company data" that indicated that part of the additions to plant were of another category and that some composite depreciation rate could possibly be used. (Staff IB, p. 24) No version of what the Company considered a proper composite rate was presented by the Company despite a Staff Data Request (Staff Cross Ex. 70) The Company witness could not point to what a proper composite depreciation would be, nor did he suggest any particular rate, stating

that it could somehow be computed from that Data Request Response, despite the lack of any numbers or methodology contained in the Data Response. (Tr. 3186)

The Company now suggests that paragraphs be inserted into the PIO, which would explain such a methodology. (ComEd BOE p. 23 and ComEd Exceptions pp. 47-48; these paragraphs are under sections “ComEd’s Response” and “Commission Analysis and Conclusion”) These methodologies were not provided in response to the Staff Data Request concerning the matter (Staff Cross Ex. 70) nor explained in the record. (Tr. 3186) Without the opportunity to investigate this new evidence, Staff vehemently opposes ComEd’s suggested additions of a methodology to the PIO.

The PIO is correct in finding that Staff’s depreciation rate is proper and is based upon the best information available. It is also correct in its finding that the Company failed to provide with any specificity an alternative or composite depreciation rate. As to this issue, the PIO should remain as written.

e. Accumulated Deferred Taxes Related to Overtime and
Alleged Premiums Paid

The language in the PIO is appropriate for the same reasons as stated in Section II. C. 6. d. As stated above, the Company now suggests that paragraphs be inserted into the PIO, which would explain a methodology for computing a composite depreciation rate. (ComEd BOE p. 23 and ComEd Exceptions p. 49; these paragraphs are under sections “ComEd’s Response” and “Commission Analysis and Conclusion”) Again, these methodologies were not provided in response to the Staff Data Request concerning the matter (Staff Cross Ex. 70) nor explained in the record. (Tr. 3186) Without the opportunity to investigate this new evidence, Staff vehemently opposes

ComEd's suggested additions of a methodology to the PIO for the computation of a depreciation rate to be used in the computation of deferred taxes.

The PIO is correct in finding that Staff's depreciation rate is proper for the computation of deferred taxes and is based upon the best information available. It is also correct in its finding that the Company failed to provide with any specificity an alternative or composite depreciation rate to compute deferred taxes. The PIO should remain as written.

- 7. Prudence of Distribution Capital Investment Costs
 - a. Effect of Alleged Imprudence on Rates
 - b. Prudence of Specific Distribution Capital Investments in Rate Base
- 8. Other Rate Base Issues
- D. Operating Revenues And Expenses
 - 1. Recommended Operating Income Statement
 - 2. Operating Revenues
 - 3. Operating Expenses
 - a. Functionalization Of Generation, Transmission, And Distribution Expenses
 - b. A&G Expenses -- Direct Assignment and Allocation
 - c. Proposed Known & Measurable Changes to Test Year Expenses
 - (i). Expense Adjustments Related To Rate Base Adjustments

(ii) "Levelization" Adjustments

a. Tree Management Expense

The Company disagrees with the PIO's acceptance of GCI's adjustment to tree management expense based on a six-year levelization period and presents arguments to refute that position and Staff's position, which is based on an eight-year levelization period. Certain of the Company's statements need further examination.

First, the Company refers to a 3.5% annual inflation factor used by Staff. (ComEd BOE, p. 30) The Company is mistaken. Staff did not use a 3.5% annual inflation factor. Staff applied the appropriate inflation factor, as identified by Wharton Economic Forecasting Associates (WEFA), for each of the years included in its levelization calculation. These factors ranged from 2.2% to 3.3%. (Staff Ex. 2.0, Sch. 2.6, p. 2) Applying a 3.5% factor to any given year would overstate the expense.

Second, ComEd points to its tree management budget for 2001 as a legitimate indication of tree trimming expense. However, the budget referred to does not exist. (Staff Ex. 16.0, p. 8) It is simply a hypothetical number calculated by the Company in response to a Staff data request. It is unreasonable to compare either Staff's or GCI's proposed adjustment to a fictitious number, and it is misleading for the Company to refer to this budget in its alternative replacement language proposal. (ComEd BOE, pp. 30-32)

Third, ComEd believes that the next most reasonable levelization period, after the three-year period included in the filing, is a four-year period, 1997-2000. (ComEd BOE, pp. 31-32) While certainly a step in the right direction, the addition of one additional year does not adequately smooth the effect of the significantly higher

expense incurred in 1999 and 2000. Staff believes that its eight-year levelization period for tree trimming expense achieves the proper level for ratemaking purposes and should be adopted by the Commission. (Staff RB, p. 22; Staff BOE, p.16)

b. Storm Restoration Costs

The Company argues that Staff's proposal and the PIO incorrectly disregard all of the changes made by ComEd in its storm restoration efforts. It further argues that its increased costs are mainly attributed to the changes in its policies and practices and changes to its accounting systems while Staff, Intervenors, and the PIO all ascribe 100% of the change to the variability of storms. (ComEd BOE, p. 34) The Company continues by inferring that Staff is being unreasonable when it will not concede that ComEd's dramatic changes have anything to do with the higher costs in 1998 – 2000. ComEd also contends that Staff is unreasonable because of its insistence on numerical quantification "even though the relation of the changes to the expenses is clear and such quantification is not possible". (ComEd BOE, p. 35)

ComEd's argument, while attempting to demonstrate that no one appreciates their endeavors to "keep the lights on", would be further heartening and effective if based in fact. Staff has never taken the position that the Company's changes to storm processes and to its accounting system, have no effect on the costs. In other words, Staff has never stated that 100% of the increase is because of storm variability. What Staff does state is this:

Because the Company may or may not have extra storm restoration costs in the years 1993 – 1997, and because of the difficulty the Company has in determining the effect new storm restoration operations has on storm restoration costs, we are left to wonder how much of the tripling of storm restoration expenses from the prior delivery services tariffs is simply due to 'mother nature.' Admittedly, the Company has not quantified how

much any of the three factors have contributed to the increase in the level of storm restoration expense. (Tr. 1960) If the Company believes there are shortcomings in the information it has and the Company is unable or unwilling to provide more comparable information, then any shortcomings resulting from the use of that information should be construed to the detriment of the Company before it is construed to the detriment of the ratepayers. (Staff IB, p. 48)

As made clear in this statement, Staff does not know how much of the increase is due to storm variability and that is because the Company has neglected to perform any kind of analysis to show how much of the increase is related to its new operations or its new accounting system. ComEd would have the Commission believe that such quantification is not possible but that should not matter because “the relation of the changes to the expenses is clear.” (ComEd BOE, p. 35) So, without performing any kind of quantification ComEd knows that the tripling of expenses is mostly due to the changes it made and any other reason, such as weather, is not a material factor. Furthermore, ComEd maintains that it is abundantly clear that these new systems and operations that ComEd is adhering to are costlier (almost triple that of their older, *inferior* systems and operations), yet the facts show that an annualized 2001 amount is not even one-third of the 1998 amount, only two-thirds of the 1999 amount, and slightly more than one-third of the test year amount. (Reflected in ICC Staff Exhibit 17.0, Schedule 17.7, p. 2, lines 8 and 9)

As argued repeatedly by Staff, it is clear that the levelization period of 1998 – 2000 is not normal, even considering the improvements in ComEd’s systems. It is unreasonable for the Company to argue that other years’ data is not comparable to 1998 – 2000 data and not perform any kind of analysis to make the data more comparable, but still expect to recover three times the amount for storm restoration costs (ICC Staff RB, p. 23) Staff’s proposal uses all the information made available

and makes a reasonable normalization adjustment that should be accepted by the Commission.

c. Reserve for Levelized Variable Storm Damage Expenses

Once again, the Company repeatedly argues that its proposal for a levelized variable storm damage expense does not violate the single-issue ratemaking doctrine (nor, is single-issue ratemaking doctrine relevant in delivery services rate cases), nor is it inconsistent with test year principles, and that the retroactive ratemaking prohibition should not be found to be applicable in this proceeding. (ComEd BOE, pp. 37, 39) Furthermore, the Company argues that because Staff has not identified anyone this proposal would harm, this is a “pareto optimal” proposal, that the Commission would be setting new policy by not adopting it. (ComEd BOE, p. 38) A final argument of the Company is that if the Commission’s final order still does not approve of the storm reserve proposal, the Order should be supplemented to state that ComEd is not foreclosed from presenting a revised storm reserve proposal in the future. (ComEd BOE, p. 37)

ComEd disagrees with the Proposed Order’s rejection of ComEd’s Storm Expense Reserve proposal. (ComEd BOE, pp. 37-40). Staff has repeatedly and convincingly demonstrated how this proposal would violate: 1) the single-issue ratemaking doctrine; 2) test-year principles and 3) the prohibition against retroactive ratemaking. (ICC Staff IB, pp. 49 – 54) Staff finds ComEd’s argument that the doctrine of single-issue ratemaking is not relevant in delivery services rate cases contradictory, as its own testimony in the record discusses why certain adjustments should not be

approved because they violate either the doctrine or the rationale underlying the doctrine. (ICC Staff Exhibit 17.0, p. 13)

In discussing the equality of the benefits of its proposed storm reserve, the Company states that Staff is unable to identify anyone the proposal would harm, and that proposals that benefit some or all but harm no one ("Pareto Optimal") and should be adopted as a matter of economic efficiency. (ComEd BOE, p. 38) Contrary to the assertion made here by ComEd, Staff witness Sant identified customers as being "harmed" or "worse off" because the benefits would be disproportionately skewed to the Company. (Tr. 1741:13 – 1745:15) Therefore, it is factually incorrect to state that Staff cannot identify harmed individuals and then use that reasoning, in part, for proving that its proposal is indeed "pareto optimal" and thus should be adopted by the Commission.

The Company explicitly states the Commission, without a legal basis, would be adopting a policy of rejecting pareto optimal proposals by not adopting this specific proposal. (ComEd BOE, p. 38) However, approval of this proposal would be akin to a new policy of reconciling over and under-recoveries of normal operating expenses, no matter what tenets of utility ratemaking, or the underlying rationale behind these ratemaking tenets, are violated, because in the Company's viewpoint, no one is *worse off*. The Company does not explain a viable legal basis for this type of new policy, i.e. ignoring ratemaking principles to approve proposals that only the Company believes are beneficial to all parties.

Staff does not agree with the Company's argument that the Commission should explicitly state that its determination does not foreclose ComEd from presenting a

revised proposal in the future that addresses Staff's concerns. Nothing in the PIO indicates that ComEd cannot present a similar or revised proposal in the future.

Staff is particularly in disagreement with ComEd's replacement language if the Commission were to supplement its conclusion with such a statement. ComEd's replacement language is as follows:

~~Based on our review of the Company's novel storm reserve proposal as well as Staff's arguments we conclude that this proposal is unnecessary and may result in an unreasonable level of reserves coupled with the potential for uneven benefits. We further conclude that this proposal may be on the cusp of being violative of the basic tenets of utility ratemaking. Accordingly, the Commission declines to adopt ComEd's proposal. should not be approved at this time. However, the Commission's determination should not be considered to foreclose ComEd from presenting a revised proposal in the future that seeks to address Staff's ratemaking concerns.~~

(ComEd BOE, p. 40) Staff believes this language does not just simply supplement the conclusion reached by the Commission, but flagrantly strips readers of a full understanding of the Commission's reasons for denying the proposal. Apparently, ComEd wants to track storm expense over and under recoveries between now and its next rate proceeding for presentation in that next proceeding, but invites the Commission to prejudge the issue only to the extent such prejudgment is clearly favorable to ComEd. As previously stated, Staff does not believe the Commission needs to explicitly state the fact that the Company is able to make similar or revised proposals in the future. Therefore, Staff recommends that no modification to this section of the PIO is warranted.

- d. Other
 - (i). Distribution Salaries and Wages

- (ii.) FERC Accounts 580, 590, 592-594 and 903
- (iii.) Salary and Wage Adjustment for General Pay Increases
- (iv.) Adjustments for Post-Test Year “Merger Savings”
- e. Other Proposed Adjustments to Expenses
 - (i) Exclusion of Incremental Expenses Related to Unicom/PECO Merger
 - (ii.) Exclusion of Audit-Related Costs
 - (iii.) Environmental Remediation Expenses
 - (iv.) Advertising Costs
 - (v.) Bank Commitment Fees
 - (vi.) Legal Expenses
 - (vii.) Charitable Contributions & Memberships
 - (viii.) Special Projects
 - (ix.) Research and Development Costs

The PIO correctly adopts Staff’s adjustment of \$3,529,000 to Research and Development Expense. ComEd maintains that Staff’s proposed adjustment to Research and Development costs, should be reduced by \$1,174,000 for “Special Projects” expenses (ComEd BOE, p. 47). Staff disagrees that this downward adjustment should be made to Research and Development Costs; Staff has already reduced the adjustment to Special Projects by \$1,174,000. Reducing it a second time is totally unnecessary, for an additional reduction of this amount would result in double counting. The only adjustment to which Staff agreed was that \$1,174,000 was in two different adjustments and eliminated the amount of \$1,174,000 in the Staff adjustment described

as “Special Projects”. Staff remains convinced that the projects for which the proposed adjustment was made were non-delivery services related.

The PIO correctly includes the \$3,529,000 adjustment for Research and Development Costs. (PIO, p. 95)

(x.) Interest On Customer Deposits

(xi.) Uncollectibles Expense

(xii.) Taxes Other Than Income Taxes

Staff’s concern is not with the legitimacy of the use tax expense, as the Company seems to imply (ComEd, BOE, p. 48), but with when and how it was recorded. It is an out-of-period expense that has been incorrectly recorded for ratemaking purposes in the test year. The Company has chosen to record the total liability, which relates to out-of-period purchases, as an expense. This is despite the fact that the Company maintains that part of the use tax relates to capitalized activities. (Staff RB, pp. 36-37) Also, the records do not substantiate the claim that ComEd is routinely subjected to tax compliance audits resulting in either an increase or decrease in tax liabilities. (Staff IB, p. 70)

While the PIO is correct in disallowing the penalty portion (interest) of use tax costs that resulted from the tax audit, the actual use tax portion for the out of test year period should also be disallowed. Staff believes that the Commission should adopt the position reflected in the replacement language of Staff’s BOE at page 27.

- 4. Prudence of Expenses
- E. Cost of Capital
 - 1. Capital Structure
 - 2. Cost of Debt
 - 3. Cost of Preferred Stock
 - 4. Cost of Common Equity
 - 5. Overall Rate of Return
- F. Cost Of Service and Rate Design
 - 1. Cost of Service Study Issues
 - a. Marginal Cost Study

ComEd presents a number of contradictory arguments against the PIO's adoption of an embedded cost standard. The Company begins by insisting that the Commission cannot simply rely on precedent for its decision on this issue, arguing, "[t]he Commission's approval of an embedded cost rate design in Docket No. 99-0117, or in delivery services rate proceedings for other utilities, provides no basis for doing so here. " (ComEd BOE, p. 51) ComEd goes on to claim that "[p]rior Commission orders are neither legal precedents nor res judicata" (ComEd BOE, p. 51). Thus, ComEd argues, the Commission cannot rely solely on precedent for its decision.

ComEd's argument is misplaced because the PIO did not rely solely on precedent for its decision on this issue. As ComEd acknowledges in its own BOE, "[t]he Order also finds that an embedded cost approach advances concerns of economic efficiency and sends economically correct price signals" (ComEd BOE, p. 50).

Furthermore, according to ComEd, “the Order concludes that ComEd presented no argument or evidence to support a marginal cost-based approach” (ComEd BOE, p. 50). Thus, the PO went far beyond the issue of precedent in finding support for its conclusion on this issue.

ComEd further confuses the issue by mining the record of Docket No. 99-0117 for arguments against the PIO’s decision in the current proceeding. ComEd begins its discussion by attempting for some unknown reason to correct the record in Docket No. 99-0117 on this issue. According to ComEd, the Commission decision in that case was somehow based in part on the Commission’s incorrect belief “that the DOE and its expert witness Dr. Swan favored” the embedded cost option (ComEd BOE, p. 52). However, the Company provides no evidence to support this assertion, nor does ComEd explain why this discussion should be relevant to the current proceeding.

ComEd continues to focus on Docket No. 99-0117 by resurrecting William Baumol’s arguments in that case concerning marginal costs. The Company presents a lengthy quote from the testimony of George Schink in the current proceeding for Midwest Generation, which, in turn, paraphrases Baumol’s testimony in Docket No. 99-0117 (ComEd BOE, p. 52). This puts ComEd in the untenable position of criticizing the ALJs for looking back to Docket No. 99-0117 while it fishes around that same docket for opposing arguments. Furthermore, by recycling arguments from Docket No. 99-0117, ComEd demonstrates that it has run out of ideas on the subject.

ComEd also tries to pull rank on the costing issue by stating that all of the Ph.D. economists testifying on this issue support the marginal cost approach (ComEd BOE, p. 52). Furthermore, ComEd notes a lack of support for embedded costs in the current

economic literature (ComEd BOE, p. 53). ComEd's claim regarding witness credentials attempts to divert attention from the lack of record support for its position. The wealth of evidence accumulated, not only in this case, but in other delivery service dockets clearly documents the myriad of problems with marginal costs. A cost theory that was developed for the artificial world of perfect competition does not travel well in the more complicated and far less perfect market for electricity in Illinois. Edison does not address the concept that the costs of the distribution system in place today and in the foreseeable future are represented by the embedded costs to be recovered through the rates to be determined in this docket. In contrast, Edison's marginal cost of service study is not based upon the actual cost of distribution equipment that is in place to meet ratepayer demands today, and is instead based upon the hypothetical cost of equipment that might be installed if the need arises. An embedded cost of service study, which uses allocation factors to determine the use of equipment that is in place, is the proper method to divide the costs of providing distribution service today. The only potential use of a marginal cost of service study is to divide the hypothetical cost of providing distribution service to some unknown location at some vague point in the not very clear future. Since this docket concerns the measurement of the cost to provide distribution service today, an embedded cost of service study is the proper method to measure today's costs to serve the delivery services rate classes.

The Company's exceptions on this issue clearly lack merit and the ALJs' acceptance of an embedded cost standard should be reaffirmed by the Commission.

b. Embedded Cost Study

2. Interclass Revenue Allocation
- G. Rate Design
1. Rider ISS
 - a. Pricing
 - b. Commission Authority to Alter ComEd's Proposal
 2. Residential Customer Eligibility for Rider PPO
 3. SBO Credit

The Company takes exception to the ALJs' adoption of an embedded cost SBO Credit on legal grounds. According to ComEd, the embedded cost standard adopted by the PO violates Section 16-108(c) of the Public Utilities Act in four different respects (ComEd BOE, pp. 57-61).

ComEd's argument defies reality. No less an authority than the Appellate Court itself has addressed this issue and found that embedded costs do not violate Section 16-108(c) of the Act (Commonwealth Edison Company v. Illinois Commerce Commission, et al., 322 Ill. App.3d 846, 854 (2001)). Despite this decision, ComEd blindly presses its legal argument against embedded costs. Staff believes the Commission should heed the wisdom of the Appellate Court and reject ComEd's legal arguments as to this issue.

In making its legal argument, ComEd demonstrates why the avoided cost standard should be avoided at all costs. ComEd notes that its avoided cost SBO credit calculation declined from 3 cents per bill in direct to a negative two cents in rebuttal (ComEd BOE, pp. 58-59). The fact that a positive credit in direct can be transformed into a negative credit in rebuttal with the help of a few well-placed assumptions

illustrates the arbitrary and capricious nature of avoided cost calculations. Furthermore, ComEd's calculation of a negative SBO credit in rebuttal reveals what the future holds for unbundling under avoided costs. It means that avoided costs will, for all intents and purposes, bring a swift end to unbundling. The Commission can avoid this scenario by reaffirming the PIO's recommendation to base the SBO credit on embedded costs.

4. Metering Service Charge (Credit)

ComEd's argument against the adoption of an embedded cost foundation for unbundling meter rates boils down to a complaint about compensation. The Company wants to insure itself against any adverse consequences under all circumstances, regardless of the direction of the metering market. According to ComEd, "[t]he embedded cost approach, therefore, improperly denies ComEd cost based rates and full recovery of its costs of providing delivery services" (ComEd BOE, p. 63).

ComEd is, in effect, demanding full financial protection when competing in the unbundling market by setting a metering price so low that potential competitors will be driven away. And even if it were to lose customers, ComEd's rock-bottom price would shield ComEd from any economic impact. Thus, the avoided cost approach would produce one-sided competition that favors ComEd at the expenses of alternative meter suppliers.

ComEd goes on to present a convoluted argument on the issue that begins with the contention that its net avoided cost approach is consistent with the decision of the Appellate Court (ComEd BOE, p. 64) and ends with the statement that "the evidence in

the record in this proceeding and the law do not permit the Commission to approve an embedded cost based approach” (ComEd BOE, p. 65).

This scatter-shot argument presents a number of problems. For one, it is a stretch indeed for ComEd to regard a ruling upholding an embedded cost methodology as any kind of endorsement of its avoided cost approach. Second, Staff would beg to differ with ComEd’s assessment of the evidence in this proceeding on the issue. The evidence clearly demonstrates that ComEd’s avoided cost methodology will derail unbundling. Third, ComEd is truly far a field in claiming that the law does not permit an embedded cost approach considering the Appellate court’s rejection of the Company’s appeal on this issue. ComEd appears to be in denial as to the legal issue.

In short, ComEd offers no concrete foundation for reconsidering the PIO’s recommendation on this issue. Therefore, the Commission should reaffirm the use of embedded costs for determining unbundled meter rates.

5. Rider TS – Transmission Service

ComEd claims that the PIO’s reliance upon ComEd’s ability to impose credit security requirements on RESs who apply for transmission service is a non sequitur because ComEd never argued that a lack of credit security requirements was part of ComEd’s rationale in the case, nor did ComEd argue that the ARTO lack the ability to impose credit security requirements upon RESs as transmission customers. (ComEd BOE, p. 67)

ComEd is not the only party to provide arguments in this proceeding. Staff has argued that ComEd’s proposal (and the language set forth in its current tariff) is

unnecessary because both ComEd and the ARTO have the ability to impose reasonable credit security requirements on the RES or other entity as the Transmission Customer, pursuant to the terms and conditions of the OATT. Furthermore, the ARTO has stated its express intent, in its OATT, to charge bad debt expense to all transmission customers (RESs or other entities) on a monthly basis when a transmission customer defaults on payments. (ARTO OATT, Vol. I Original Sheet No. 283, Schedule 10, Administrative Fee, Section (4)) This argument is relevant because it has not been demonstrated in this case that current or proposed credit security requirements are unreasonable. ComEd's approach establishes a policy that encourages transmission providers to discard due diligence and virtually ignore the credit security requirements of a RES because the risk of non-performance is transferred to uninformed retail customers by the ComEd retail delivery services tariff.

ComEd's claims that it is just trying to promote retail competition by avoiding the imposition of needlessly expensive credit security requirements upon a RES, this is not an appropriate policy when it comes at the expense of uninformed retail customers. A RES should negotiate this liability with a retail customer and thus allow the informed retail customer to determine whether the potential benefits are worth accepting the risk of the RES' non-performance.

The Commission should ask the question, "If ComEd's argument regarding the benefit to retail competition is true, then why must this condition be imposed upon retail customers in the ComEd tariff?" It stands to reason that a RES could and should advance the same argument as ComEd to a retail customer in negotiating for their business. However, the task is not so simple when one must explain and convince

retail customers of the benefit to them of accepting the risk of the RES's non-performance. As Staff has argued, procuring transmission service is a complex task that requires specific professional expertise and it is not credible to expect retail customers, other than a very small minority, to have any understanding of this service, i.e., it is not credible to claim that retail customers can procure transmission service via the OATT on their own. Moreover, since retail customers are likely to be served in aggregation by a RES, it is impossible for a retail customer to determine the extent of their liability for the RES' non-performance because retail customer A has no knowledge of the usage of retail customers B through Z who are served by the same RES. The nature of the service and its extreme complexity should convince the Commission that the liability for payment should remain with the RES or other entity responsible for procuring service as the transmission customer.

The collapse of Enron demonstrates that even the largest suppliers in the energy industry are not guaranteed to remain in business, i.e., the risk of non-performance by a RES is real. This risk should not be transferred to an uninformed retail customer when the same RES is the transmission customer and has the knowledge and expertise to procure transmission service via the OATTs and the OASIS. ComEd's position, if carried to its logical extension, is that it is better to lower Enron's credit cost, at the expense of retail customers, then it is to hold Enron accountable for reasonable credit security requirements that mitigate, but do not completely eliminate, the cost of Enron's non-performance to retail customers.

Potentially lowering the cost of doing business to a RES may be good for the RES, but it is not necessarily good for retail competition when it is accomplished by

shifting these costs to uninformed retail customers who have no way of mitigating the cost of non-performance of the RES.

6. 24 Month Return To Bundled Service Requirements

III. Terms and Conditions Issues

A. SBO Credit Eligibility (Customers With Past Due Bundled Service Balances)

The ARES Coalition urges the Commission to not adopt the single billing plan in which customers with unpaid bundled balances would be prohibited from using single billing services until the unpaid balances is paid in full. They cite the Commission's decision in the "Uniformity" proceeding, in which the Commission determined that utilities are responsible for collecting unpaid bundled balances from delivery services customers (ARES Coalition BOE, pp. 71-72).

Staff supports this plan primarily because other options for addressing this issue could be viewed as cost-prohibitive. Staff also noted, however, that the viability of the plan depends on its acceptance by all parties, particularly suppliers. Staff indicated that a lack of general support for the plan could necessitate the Commission revisiting the issue yet again (Staff Ex. 24.0, p. 3). For purposes of this proceeding, Staff recommends that the Commission adopt the plan as supported by ComEd and Staff. Staff recognizes, however, that the issue may arise in the future.

- B. Enrollment Issues
 - 1. Electronic Signatures
 - 2. Term of Service
- C. Release and Use of Customer Specific Information
- D. Off-Cycle Or Non-Standard Switching For Residential Customers
- E. General Account Agency Issues

The ARES Coalition views the General Account Agency form as unnecessary and a barrier to competition (ARES Coalition BOE, p. 73). However, Staff views the form as a relatively efficient means to inform customers of the risks of hiring an agent to work on their behalf. Moreover, ComEd, like other utilities, currently requires similar documentation of the customer/agent relationship (Staff Ex. 24.0. p. 3). This form merely standardizes that documentation while also putting customers on notice that the customers who hire agents are nevertheless still responsible for paying their electric bills should the agents fail to fulfill their duties to pay the bills in a timely fashion.

- F. Value-Added Aggregation Services
- G. Collection of FERC Charges Under DSTs

CONCLUSION

WHEREFORE, for the reasons set forth above and those previously stated in its briefs, the Staff of the Illinois Commerce Commission respectfully requests that its modifications to the Administrative Law Judges' Proposed Interim Order be adopted.

Respectfully submitted,

STEVEN G. REVETHIS
JOHN C. FEELEY
Office of General Counsel
Illinois Commerce Commission
160 North LaSalle Street
Suite C-800
Chicago, Illinois 60601
(312) 793-2877

Counsel for the Staff of the
Illinois Commerce Commission

March 4, 2002